

CONSUMER ADR IN THE EU: THE CHOICE RESTS WITH BUSINESS

Professor Dr Christopher Hodges¹

January 2012

The Commission's Proposals on Consumer ADR

On 29 November 2011 the European Commission adopted a Communication and two legislative proposals on consumer ADR and ODR.² These were the latest steps in the development of consumer protection that started in the 1960s, and of the place of ADR within consumer protection that has emerged since the mid-1990s. The proposals form a major policy watershed for the relations between consumers and business, and vice versa. In summary, the proposals by DG Sanco would create a pan-EU framework of consumer ADR bodies, operating within inter-linked national frameworks. Each Member State would have a residual ADR capability that would catch every possible type of ADR claim.

What is Consumer ADR?

ADR is widely known in some Member States, meaning mediation or other techniques (eg early neutral evaluation) for claims that are otherwise brought through the court system. However *consumer ADR*, for resolving disputes between consumers and traders (B2C) in practice means the totally separate world of consumer ombudsmen or related procedures, such as dispute resolution procedures attached to business codes of good practice. Consumer ADR procedures are usually closely related to companies' in-house customer care functions. (No fault compensation schemes for personal injuries are different but related.) Many consumer ADR systems are quite new, and their existence and structures differ considerably across EU states.

Why ADR?

Consumer ADR systems have existed in some countries for 40 years. Nordic countries are well familiar with sectoral Boards for resolving disputes, often with a central residual Board (in Sweden the ARN). The Netherlands has constructed an integrated system of sectoral Geschillencommissie, run by a single Foundation (DGS). Central European states often have a dispute resolution function located

¹ MA PhD FSALS; Head of the CMS Research Programme on Civil Justice Systems, Centre for Socio-Legal Studies, University of Oxford; Erasmus Professor of the Fundamentals of Private Law, Erasmus University, Rotterdam; Life Member, Wolfson College, Oxford.

² Alternative Dispute Resolution and Online Dispute Resolution.

within a regulatory body (eg the State Consumer Rights Protection Authority of Lithuania, or the Trade Inspection in Poland).

However, consumer ADR in some states has grown piecemeal and relatively recently, and without the existence of a unified national scheme. Leading examples are:

- the United Kingdom, where the Financial Ombudsman Service is statutory; private sector ombudsmen are required for some sectors such as telecoms, energy and lawyers, and various private dispute resolution schemes exist, such as for ABTA³ and under the OFT's CCAS for motor vehicles and others);⁴
- Germany, where there are some little-used complaint schemes within regulators (Bundesnetzagentur, Bundesbank) and a limited but growing number of private sector ombudsman, such as for banks, insurance and transport: the Insurance Ombudsman model works well and has been copied in some transport sectors;
- France, where there are some médiateurs located within regulators (banks), many within companies, only one statutory médiateur (energy, in competition with companies' médiateurs), and some sectoral médiateurs (telecoms), but also a network of local government-located complaint systems.
- Spain, where systems are based on arbitration rather than mediation.

The general picture across Europe is, therefore, highly diverse and confused. Some systems attract high levels of contacts from consumers, since they have high profile and levels of trust, and offer user-friendly services. Other systems are little used, little known, and not trusted.

However, wherever consumer ADR systems work—i.e. they are used by consumers in significant numbers—they have certain clear features. **They have high profile; they are trusted by consumers; they attract high levels of requests for information, which usually far outnumber disputes, and so can resolve customer issues quickly before escalation; they provide good sources of feedback information for businesses on products, services, markets and competitors; they are far cheaper and more desirable than courts; and they are paid for by business.**

Our empirical research has found that consumer ombudsmen work where business pays for them. It has found that business sectors often switch from being against ADR systems to being strongly in favour of them—and at that point they are prepared to agree in advance to accept the non-binding recommendations of ombudsmen, and to pay for the ombudsmen system, so as to make the ADR system more attractive to consumers by having no cost and being swift and effective.

³ The UK travel agents association.

⁴ The Consumer Code Approval Scheme operated by the UK Office of Fair Trading. See *Consumer Codes Approval Scheme: Core Criteria and guidance 2008*, available at: http://www.offt.gov.uk/shared_offt/Approvedcodesofpractice/oft390.pdf

In short, alternative dispute resolution services have usually been established as an alternative universe to the courts, since courts and lawyers have failed to provide user-friendly access to justice for multiple small value issues that arise between consumers and traders. The ‘consumer ADR’ universe has developed—ultimately led by businesses—as a more desirable modern technique. Further, consumer ADR systems offer not only cheap, swift and effective dispute resolution but also a range of additional benefits for business, markets and consumers.

The best ombudsmen systems adopt the techniques of mediation and sometimes adjudication to their structures, and so can deliver the well-known advantages of mediation, such as being low key, low cost, adopting flexible solutions for problems, restoring relationships between consumers and business, avoiding damaging confrontations and loss of consumer confidence and business reputation, avoiding lengthy adverse publicity in the media.

Importantly, consumer ombudsmen can be set up so as to handle mass disputes or issues, especially if designed to inter-relate effectively with companies’ in-house customer service departments, with regulators, and with courts. Consumer ombudsmen can—and some already do—respond to multiple consumer claims about similar issues. In other words, ombudsmen can replace the need for collective court actions, if they are established properly.

The Class Action/Collective Redress Debate

A debate has been going on between consumers, governments, lawyers, judges and business about whether there is a need to introduce a class action rule into civil procedure. Judges in every country see a need to have a rule when they become faced with mass aggregated claims. Governments also sometimes see a need to adopt a class action as a regulatory technique, to control business behaviour. In circumstances where public funds are limited, privatisation of law enforcement through enlisting ‘private attorneys general’ (as they are known in U.S.A.), funded by contingency fees or third party investment funding, is highly attractive to governments.

To date, fourteen EU Member States have introduced some sort of collective action, and the technique is spreading: drafts exist in Malta and Lithuania. Some governments have started extending private funding for litigation: leading examples are Poland (in its Class Action Law) and the U.K. (implementing ‘Damages-Based Agreements’ and ‘Qualified One Way Cost Shifting’, as recommended by the Jackson Costs Review). These trends at national level are likely to continue.

At EU level, there has been lengthy debate about introducing collective actions for consumer claims, and for competition damages. Other fields may follow. Business has put enormous effort and arguments into objecting to collective redress, and met with considerable success in recent years. But the debate is far from over. In 2012, the European Commission is due to publish its ‘general principles’ on how collective actions should work. That is likely to be immediately followed by a proposal for collective actions in the competition field.

The existence of a collective action procedure, coupled with the availability of funding for litigation and favourable costs rules, would encourage lawyers and funders to bring large collective claims seeking damages to enforce *any* provision of consumer protection law—as occurs in U.S.A. The fact that consumer law is not enforced in that way now is no guarantee that lawyer/funder behaviour would not change if the financial incentives were to change.

The Relationship between Consumer ADR and Collective Redress: The Choice for Business

In relation to consumer redress, both individual and collective, the Commission has been persuaded for the present to pursue a policy of focusing on ‘consumer ADR’ systems in preference to collective actions as a means of delivering consumer redress. That policy has led to the legislative proposals of November 2011.

This situation may represent a watershed opportunity for the development of a modern balanced legal system. If business shows that it is seriously in favour of consumer ADR systems, the extensive and costly litigation might be avoided. If business is against the ADR proposals, or equivocal about them, then the likelihood will be both that existing consumer ADR systems will not be developed adequately and also that court-based private enforcement, with collective actions, will spread.

The link between class actions and ADR has been made explicitly in France. In 2009, the French Consumer Minister delivered a stark ultimatum to business: if you do not create an effective ADR system, I will introduce a generic class action mechanism. This has led to business putting considerable effort behind the development of consumer *médiateurs*, and a new national Charter on ADR. (That Charter has many good points, but in my view it is not robust enough in some respects.)

Thus, the choice is between an effective consumer ombudsman system and a class action. Disputes have to be resolved one way or another. If it is going to be through the courts, the spread of class action mechanisms is inevitable. If it is not going to be through class actions in the courts, then a viable effective alternative has to be identified and made to work. The viable alternative is a pan-EU system of consumer ADR as now proposed by the Commission.

The Problem

The Commission has proposed both a policy and a structure that would enable an effective pan-EU system of consumer ADR to be constructed. But some leading Member States are likely to oppose it—unless the business community tells them that business is in favour of the proposed system, and will pay for it.

Governments are concerned about two issues. First, although the larger States are in general in favour of consumer ADR systems, which exist in some sectors, they do not currently have a single unified national ADR system (unlike the Nordics, CEE States and Netherlands) that can operate as a residual catch-all for *all or any* type of consumer dispute. Secondly, they rightly do not want to impose unnecessary costs on

public or business funds, for example by requiring there to be a single national catch-all ombudsman system.

Many general consumer trading companies consider (often rightly) that they have highly effective in-house customer care departments that deal swiftly, cheaply and effectively with all customer issues. Accordingly, they argue that they do not need (or need to pay for) any external ombudsman system. However, some arguments that need to be considered are:

1. If in house systems are indeed effective, the need for any external system will be low. Ombudsmen data clearly show that it is traders with poorer standards of customer care that are named in complaints: cost structures can be built accordingly, so as to load the (low) cost onto those who receive high levels of complaints.
2. ADR schemes have traditionally been available only for members of trade associations, and not for 'rogues', but the behavioural power of an ADR scheme can be applied to rogues if the scheme is made mandatory, by law. In that way, it can operate to clean up a market, and improve the competitive position of strong businesses.
3. Even companies that have high levels of customer care can sometimes benefit from having an external long-stop. It catches issues that might otherwise go to court, or deals with intransigent customers. It can provide useful market information on an aggregated basis or about competitors.
4. General consumer businesses have a small number of claims currently that go to court each year. They are best handled by small claims mediation, or an efficient court system in some countries. If those claims were transferred to ADR systems, and resolved quickly and at low cost there, that would be satisfactory. The cost could simply be switched from the court budget to the ADR budget. The key objective would be to design the ADR system so that it did not encourage an increase in unjustified complaints.
5. If business does not support an effective consumer ADR system, the threat that collective action procedures will be introduced is very real. If that happens, large companies will certainly be sued in large, costly and damaging court actions, irrespective of merits.

The Proposed Policy

The Commission, Governments and MEPs clearly favour the development of ADR for resolving disputes. However, the viability of the current ambitious proposals for a comprehensive consumer ADR system lies to a significant extent with business. If business indicates that it will support ADR as a way forward for redress, then the proposals will proceed in the short term and can be expected to develop as a strong alternative to courts and private litigation. If the converse, then collective actions are far more likely to spread.

The recommendation, which has already been adopted by members of the European Justice Forum, is that business should:

- Tell governments that it supports a balanced system of consumer ADR, provided it has certain adequate safeguards.
- Insist that there is a general rule that every consumer complaint must first be referred to the trader, who must have an adequate opportunity to resolve it.
- Negotiate an understanding that in return for business support for effective consumer ADR systems, governments will not permit collective actions, or private litigation funding arrangements.
- Insist that if consumer ADR systems are to be paid for by business, business should have a strong role in their design and oversight.